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BEFORE THE ARIZONA CORPORATION COMMISSION

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Arizona Corporation Commission

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IN THE MATTER OF THE COMPETITION
IN THE PROVISION OF ELECTRIC
SERVICES THROUGHOUT THE STATE
OF ARIZONA

DOCKET NO. U-0000-94-165

NATIONAL RURAL UTILITIES
COOPERATIVE FINANCE
CORPORATION'S COMMENTS

The National Rural Utilities Cooperative Financing Cooperative (CFC) submits these comments in response to the Commission's draft proposed rule on Retail Electric Competition.

CFC is the national financing cooperative for America's nearly 1,000 consumer-owned, not-for-profit electric cooperatives. These electric cooperatives provide electric service to portions of 2,600 counties in 46 states. They serve 30 million people and their service territories cover 70 percent of the land area of the United States. Each electric cooperative is owned by the local consumers who receive electric service from the cooperative and is controlled by a board of directors elected by these consumer/owners.

CFC was established by the electric cooperatives in 1969 and is owned by these cooperatives. The purpose of CFC is to provide private market capital to electric cooperatives. CFC's role in furnishing this private capital is specifically referenced in Federal Law (7 USC 936). Today CFC has more than \$7 billion in outstanding loans to electric cooperatives throughout the nation.

In general, CFC, as a private lender to Arizona's electric cooperatives, is concerned that the draft proposed rule would substantially reduce CFC's loan security by: (1) restricting the cooperatives' ability to charge rates sufficient to cover their costs, including debt service; and (2) effectively voiding the effect of the contract under which all of the electric power requirements of consumer/owners of five of Arizona's distribution cooperatives is provided by the Arizona Electric Power Cooperative. Over the past two and a half decades, CFC has made numerous loans to Arizona's electric cooperatives and today has more than \$130 million in long term financing outstanding to these cooperatives. CFC's decisions to extend credit to Arizona's cooperatives were based upon the commitment of these cooperatives to accept their obligations to repay these loans and upon the contractual relationship between Arizona's distribution cooperatives and Arizona Electric Power Cooperative. These obligations which underpin the security for CFC loans were agreed to by consumer/owners of these Arizona cooperatives who were elected by other consumer/owners to serve as cooperative board members and thereby act on behalf of all consumer/owners of these cooperatives. We urge the Commission to modify the draft proposed rule to ensure that Arizona's cooperatives are able to honor their obligations to CFC and other creditors which were entered into by democratically elected boards.

Our specific comments are as follows:

1. Allow Recovery of "Stranded Investment" Sufficient to Honor all Debt Obligations.

The draft proposed rule does not explicitly provide for the recovery of "stranded investment". It merely provides that "an Affected Utility may request Commission approval of exit fees, distribution charges, or other means of recovering Stranded Investment....". The proposed rule also prohibits the recovery of Stranded Investment after December 31, 2004.

When CFC decided to extend credit to Arizona's electric cooperatives this was based on the willingness of these cooperatives to accept the obligation to repay this financing and upon the fact that these decisions were made by individuals elected by the very consumers who would repay these loans through their electric rates. These CFC loans are made for a repayment term of 35 years, because the facilities being financed have a long useful life. The draft proposed rule ignores the useful life of the assets financed and implements an arbitrary 2004 cutoff date for recovery of "Stranded Investment". We suggest that any cutoff date for investment recovery should be based on the expected useful life of the investments.

CFC urges the Commission to modify the proposed rule in R14-2-xxx7 by specifically allowing "Stranded Investment" recovery sufficient to ensure that cooperatives have adequate revenues to honor their debt obligations and by removing the arbitrary 2004 cutoff date.

2. Preserve the Sanctity of the Wholesale Power Requirements Contracts Between Electric Distribution Cooperatives and Arizona Electric Power Cooperative.

The financial strength of a rural electric generation and transmission (G&T) cooperative, like Arizona Electric Power Cooperative, is dependent upon the legal contractual relationship that it has to provide the wholesale power needs of all consumers served by its distribution members. Rural electric G&T cooperatives are creatures of their distribution cooperative members. G&T cooperatives are not simply vendors of wholesale power to their distribution members. These G&Ts are owned by and exist to provide the wholesale power needs of their distribution cooperative members. Their boards of directors are comprised of individuals elected by the distribution cooperatives.

CFC is concerned that the draft proposed rule would nullify the effect of the wholesale power contract by permitting -- even encouraging -- consumer/owners of distribution cooperatives to bypass their G&T cooperative and purchase power from other sources. If this occurs, the financial underpinning of these G&Ts will be jeopardized. Such an action by the Commission would punish lenders like CFC for their good faith in providing financing to Arizona's electric cooperatives based on commitments of co-op directors elected by co-op consumer-owners.

We strongly recommend that the proposed rule be modified in R14-2-xxx4 to ensure that it does not establish a system under the name of "Retail Electric Competition" that would have the same consumers who -- through their elected co-op directors -- chose to form a G&T (and accept a wholesale power requirements contract as necessary condition to attract financing) then bypass that same G&T and jeopardize its ability to repay its debt obligations incurred to meet the power needs of these same consumers.

The draft proposed rule provides in section R14-2-xxx4(F) that:

"Consumers served under existing contracts are eligible to participate in the competitive market prior to expiration of the existing contract only if the Affected Utility and the consumer agree."

CFC believes that this same requirement should be applied to consumers served by an electric distribution cooperative that has a wholesale power requirements contract with a G&T cooperative. These consumers

are the owners of their distribution cooperatives and through their fellow consumer/owners who they elect as co-op directors they have established G&T cooperatives which have received financing based on their all requirements wholesale power contracts. The entire structure of consumer-owned cooperatives rests upon the foundation of living up to obligations made in good faith by co-op directors duly elected by consumer-owners. This is similar to the obligation referenced in R14-2-xxx4(F) that exists in the case of a contract for electric service between a consumer and an Affected Utility. We urge the Commission to clarify R14-2-xxx4(F) to specify that agreement between the consumer and its electric cooperative is required before a co-op consumer can "participate in the competitive market prior to the expiration" of the wholesale power requirements contract between the consumer/owner's distribution co-op and its G&T cooperative.

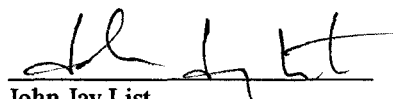
3. Remove Cooperatives From the Definition of Affected Utilities if Municipal and other Publicly-owned Utilities are Excluded.

The draft proposed rule would subject electric cooperatives to the new "Retail Electric Competition" rule, but would (under R14-2xx11) permit municipal and certain other publicly-owned utilities to voluntarily decide whether to participate.

CFC urges the Commission to change R14-2xx11 of the proposed rule to provide the same options to rural electric cooperatives as are available to municipal utilities. Cooperatives are similar to municipal utilities in that both are locally-owned and controlled and both operate as not-for-profit entities. However, by any measurement, rural electric cooperatives are disadvantaged relative to municipal utilities. For example, cooperatives operate with substantially lower consumer densities than municipal utilities (6 consumers per mile of line for cooperatives compared with 48 for municipal utilities on a nationwide basis, and 8.5 consumers per mile for Arizona electric cooperatives compared with 34 for Arizona municipal utilities). Cooperatives have lower revenues per mile than municipals (\$7,038 vs. \$72,300 on a nationwide basis, and \$13,800 for Arizona co-ops vs. \$58,830 for Arizona municipals). Cooperatives also have far lower load factors and serve fewer large commercial and industrial consumers than municipal utilities.

CFC believes that there is no public policy objective that will be served, nor any test of fairness satisfied by giving municipal utilities the option of voluntarily deciding whether to participate in this new policy, while denying that option to consumer-owned electric cooperatives.

We appreciate this opportunity to comment on the Commission's draft proposed rule on "Retail Electric Competition", and we would appreciate the opportunity to discuss this matter with you.



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